WASHINGTON LEGISLATURE ADOPTS INCOME TAX AND CHANGES TO ESTATE TAX

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US Tax Alert

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RECENT CHANGES TO WASHINGTON TAX LAW FOLLOWING 2026 LEGISLATIVE SESSION

The Washington state legislature has adjourned for 2026, and key tax changes are in store if Governor Bob Ferguson signs several tax-related bills into law, and if those tax changes then survive expected legal challenges. The legislature passed a new state income tax (known as the “millionaires' tax” because it provides a standard US$1,000,000 deduction, effectively limiting application of the tax to individuals whose income exceeds US$1,000,000), while also passing a bill to undo the 2025 increases to Washington's estate tax rates. The new legislation adds to a rapidly evolving Washington state tax environment, which had already seen the adoption of a new Washington capital gains tax in 2021 (and a subsequent rate increase in 2025 for capital gains over US$1,000,000).

Our firm is closely monitoring the impact of these bills and will supplement this information as these issues progress.

ADOPTION OF STATE INCOME TAX (THE “MILLIONAIRES' TAX”)

Starting on 1 January 2028 (taxes to be due beginning in 2029), Washington taxpayers would be subject to tax on Washington income at a 9.9% rate. A US$1,000,000 standard deduction from Washington base income would apply and would be indexed for inflation every two years.

Who Is a Washington Taxpayer?

The new Washington income tax would apply to all income of individuals who are Washington state residents as well as to income of nonresidents derived from Washington sources.

A person is a Washington state resident for purposes of the income tax if either (1) Washington is his or her domicile during the year (unless he or she kept no Washington home, kept a home outside of Washington all year, and spent no more than 30 days physically present in Washington), or (2) he or she is not domiciled in Washington but maintained a Washington place of abode and were physically present in Washington for more than 183 days during the year. This mirrors the residency test applicable to the Washington capital gains tax.

How Would Washington Income Be Calculated?

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Washington base income for purposes of determining the amount of the tax would be calculated starting with a taxpayer's federal adjusted gross income (AGI), which is then subject to various adjustments (e.g., interest income from non-Washington state debt obligations and state and local taxes that were excluded or deducted from federal taxable income are added back). Taxpayers would deduct federal long-term capital gains and add in net Washington long-term capital gains.

How Would the Deduction Be Applied?

After determining Washington base income, taxpayers would apply the standard US$1,000,000 deduction. Importantly, married couples and state-registered domestic partners would have the same standard deduction of US$1,000,000 of income regardless of joint or separate filing status.

Charitable deductions against Washington base income would be capped at US$100,000 (including for joint filers). Unlike federal income tax, where charitable deductions are calculated on a percentage of AGI, charitable contributions in excess of US$100,000 would not be deductible for purposes of calculating Washington income tax liability.

What Would Be the Impact on the Washington Capital Gains Tax?

The income tax bill would not eliminate the Washington capital gains tax. Instead, it would provide a credit for Washington capital gains taxes paid. This interaction between the two taxes could have the effect of eliminating the benefit of the lower rate on Washington capital gains up to US$1,000,000, which are currently taxed at 7%.

What Other Sources of Income Are Included?

Washington base income for purposes of the millionaires' tax includes income that is allocated to individuals on Schedules K-1 from pass-through entities, such as S corporations and partnerships. Pass-through entities may elect to pay the Washington tax at the entity level, which could enhance Washington taxpayers' ability to deduct Washington state income taxes on their federal returns.

Does the Tax Apply to Nonresidents?

Nonresidents would also be subject to the tax on Washington-source income, including wages and other compensation, income attributable to any business, trade, profession, or occupation carried on within the state; and rental income attributable to Washington property. There is a safe harbor for service income earned by nonresidents who spend five or less days performing services in-state during a calendar year (excluding compensation for athletes).

When Would the “Millionaires' Tax” Apply?

As noted above, the relevant period would begin 1 January 2028, with the applicable taxes due beginning in 2029. This is subject to the bill becoming law; in a press release after passage of the bill by the legislature, Governor Ferguson indicated that he would sign the bill as passed. Once signed into law, the millionaires' tax is expected to face legal challenges—at least one organization, Citizen Action Defense Fund, has stated that if the bill becomes law, it is “prepared to take prompt legal action.”

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WASHINGTON ESTATE TAX RATES REVERTED BUT EXEMPTION FROZEN

Starting 1 July 2026, SB 6347 would reduce the estate tax rate increases that went into effect 1 July 2025. A late amendment to the bill has the effect of once again freezing the estate tax exemption.

If the bill is signed into law, the rates would revert (as noted in the table below[1]) back to a range between 10%–20%, depending on the value of the decedent's Washington taxable estate (referring to the amount over the available exemption).

Washington Taxable Estate Value	Pre-2025 Rate and New Rate (After 1 July 2026)	Current Rate (Through 30 June 2026)
US$0 to US$1M	10%	10%
US$1M to US$2M	14%	15%
US$2M to US$3M	15%	17%
US$3M to US$4M	16%	19%
US$4M to US$6M	18%	23%
US$6M to US$7M	19%	26%
US$7M to US$9M	19.5%	30%
US$9M+	20%	35%

While last year's SB 5813 implemented an inflation index, that inflation index would revert under the recently passed bill to an inflation index that does not exist (the former Seattle-Tacoma-Bremerton index). Effectively, while the legislature elected to maintain the increased exemption amount of US$3,000,000 per individual, the exemption would remain frozen with no valid inflation index against which to calculate an increase.

For decedents dying on or after 1 July 2026, the available exemption would revert to US$3,000,000. The exemption would continue at US$3,076,000 for estates of decedents who died between 1 January 2026 and 30 June 2026 (as a result of 2025 adjustments and prior to the new bill taking effect).

UNDERSTANDING THE IMPACT

The firm's Tax and Estate Planning and Trusts & Estates practice groups are well positioned to discuss these bills' impacts on each client's unique circumstances, as well as planning opportunities, and our policy team continues to monitor these developments. Please reach out to your contact at the firm today to discuss how we can provide insight or assistance.

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FOOTNOTES

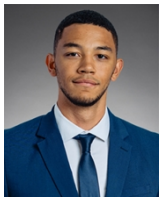
[1] For each rate tranche, there is a base amount of tax, and the rate applies to any amount in excess of the Washington estate tax exemption.

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